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October 10, 1997

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

BY HAND DELIVERY

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, N.W.
Room 222
Washington, D.C. 20554

Re: **Notice of Ex Parte Presentation; Federal-State - Joint Board on Universal Service; CC Docket No. 96-45**

Dear Mr. Caton:

On October 10, 1997, the undersigned, representing EDS Corporation, and Allen Miller of EDS Corporation, met with John Nakahata, Acting Deputy Chief of the Common Carrier Bureau and Valerie Yates of the Common Carrier Bureau, to discuss certain aspects of the universal service fund as it relates to private operators, including systems integrators. The attached hand-outs, in addition to the pleadings of EDS already filed in CC Docket No. 96-45, cover the points discussed at the meeting.

Pursuant to Section 1.1206(b) of the Commission's rules, an original and one copy of this letter and attachment are being filed with the Secretary. Please date stamp the "stamp and return" copy of the letter for return by the messenger.

If you have any questions concerning this submission, please contact the undersigned.

Sincerely,

Randolph J. May

Randolph J. May

Enclosure

cc: John Nakahata, Common Carrier Bureau
Valerie Yates, Common Carrier Bureau

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List ABCDE

Jeffrey M. Heller
President and Chief Operating Officer

EDS

September 26, 1997

The Honorable Reed Hundt
Chairman
Federal Communications Commission
1919 M Street, NW
Washington, DC 20554

Re: Ex Parte Presentation; CC Docket No. 96-45

Dear Chairman Hundt:

I am writing regarding the Commission's recent Universal Service Order. For the first time, EDS and other systems integrators will be subject to new and substantial regulatory burdens by requiring us to pay directly into the Universal Service Fund. This additional complexity has been imposed despite the fact that we already contribute to support universal service in a much less burdensome manner. We currently pay for universal service through the rates which we pay to our common carrier for the use of their telecommunications facilities. We expect to continue to contribute to universal service in a cost-effective and reasonable manner.

I would appreciate your review of what we believe to be an unintended situation. The issuance of some communication that clarifies the intention of the Commission to retain the current methodology for systems integrators to contribute to the Universal Fund would rectify this problem. I feel that such an action is justified for the following reasons:

- This order subjects an internationally competitive segment of the U.S. services industry to unnecessarily burdensome and costly regulation.
- Systems integrators already contribute to the Universal Fund through a more efficient mechanism and any additional revenue generated by direct payments is marginal.
- Due to contractual obligations this order will require systems integrators to make double payments to the Universal Service Fund.

New Costly and Burdensome Regulation

As you are well aware, the U.S. information services industry is one of the most competitive industries in the world and our trade flow is substantially positive. Certainly a

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contributing factor to this good news is the historic position of the U. S. Government and your agency to leave this industry relatively free of unnecessary rules and regulation. Further, this position has been reinforced very recently by the Administration's Global Electronic Commerce Framework.

The Universal Service Order requires systems integrators, for the first time, to report revenues for their provision of basic telecommunications services to their customers. Since the provision of these services is typically incidental to other types of unregulated services incorporated into our systems integration contracts, we do not currently maintain the accounting systems and administrative mechanisms which allow us to break these costs out in an efficient and cost-effective manner. There has been no need to do so in the past, and to create and maintain these systems now would add considerable administrative cost to our intensely globally competitive industry.

In the short term, we feel these costs will make us much less competitive with non-U.S. firms. In the longer term, we feel that other countries will follow the U.S. lead and force the entire industry to install and maintain a complex reporting infrastructure. This will make our services more costly which will have a dampening effect on the industry and, possibly, on entire economies. As we argued in the GBT negotiations, the telecommunications industry and those which depend on it had an important and beneficial impact on global economies.

Current Contribution Methodology Is More Efficient

Systems integrators such as EDS currently contribute to the Universal Service Fund through the rates which we pay for the telecommunications facilities we procure from common carriers. Over the years as our telecommunications needs have grown exponentially due to new technology and new services, this has amounted to substantial contributions to the Fund by systems integrators. Due to the nature of our business, this has occurred at the same time that, as a portion of our total contracts, basic telecommunications services which we provide are only incidental to our core business.

While our contributions have been significant, the current collection mechanism is not overly burdensome or time consuming. The necessary accounting systems and administrative mechanisms are already in place by the carriers and well understood by them. On the other hand, direct payments by systems integrators will result in only marginal, if any, increased contributions to the Universal Service Fund while imposing substantial new costs.

Contractual Obligations Result in Double Payments

One characteristic of the systems integration industry is relatively long-term contracts. Thus, EDS, like other systems integrators, has negotiated contracts in place with both our carriers and our customers. The practical impact of this Order is that we end up making double payments into the Universal Service Fund.

Payments are required to be made directly by systems integrators as a result of the Order. At the same time, the contracts we have negotiated with our carriers have the universal service payments anticipated by the carriers embedded in them. While the Commission stated an assumption that the carriers would pass their reduction in cost on to their customers, who themselves are subject to making payments, they have been unwilling to renegotiate these contracts to date.

Our contracts with our customers which include the provision of services subject to the Order, require us to provide these services at a negotiated rate. Like the carriers, our customers have been unwilling to renegotiate these terms to permit us to pass through the additional costs imposed by the Commission.

Until such time as these contracts expire and new ones are negotiated, EDS, like other systems integrators, will be making double payments into the Universal Service Fund.

Conclusion

EDS has participated actively in the reconsideration phase of the Universal Service Proceeding. I sincerely appreciate the opportunity to present our views to you on this very important matter to EDS and to other systems integrators. I am sure that you will consider our views carefully and am hopeful that you will resolve the issue in a way which does not disadvantage this very important and intensely competitive industry.

If you have any questions or need additional information, please contact Allen Miller in our Office of Government Affairs at +1 202 637 6742. He can also be reached via e-mail at allen.miller@oga.eds.com.

Sincerely,

Jeffrey M. Heller

JMH/azm

cc: Acting Secretary William Caton (2 copies) for CC Docket No. 96-45
The Honorable James H. Quello
The Honorable Rachelle B. Chong
The Honorable Susan Ness

Ex Parte Submission of the Ad Hoc Telecommunications Users Group, EDS Corporation, the Information Technology Association of America, and International Business Machines Corporation, CC Docket 96-45

THE COMMISSION SHOULD RECONSIDER ITS DECISION TO IMPOSE UNIVERSAL SERVICE PAYMENT OBLIGATIONS ON SYSTEMS INTEGRATORS AND OTHER PRIVATE SERVICE OPERATORS

- **Systems integrators support the goal of universal service. They will make contributions to universal service through the rates that they pay to common carriers for telecommunications services. However, requiring these providers to make direct payments to the universal service fund raises significant problems. This approach:**

  -- would impose significant new costs, with no corresponding public interest benefits;

  -- would impose a form of common carrier regulation on previously unregulated competitive operators;

  -- would result in systems integrators making "double payments";

  -- is inconsistent with congressional intent; and

  -- could result in reduced services for business customers.

- **Requiring systems integrators to make payments to the universal service fund in the same manner as common carriers will impose significant new costs, while providing no new benefits.**

  -- Systems integrators will incur significant costs.

    + Unlike common carriers, systems integrators do not classify revenue as telecommunications or non-telecommunications. Nor do they separate interstate and intrastate revenues.

    + To comply with the Order, systems integrators will be required to fundamentally restructure their business operations to reflect these regulatory distinctions.

+ This will impose far more significant costs than the Commission anticipated. For some firms, these costs may outweigh the size of their USF payments.

-- Requiring systems integrators to make payments to the USF will not generate any additional revenue for universal service, and will have almost no effect on the size of the carriers' contributions.

- **Requiring systems integrators to make payments directly to the universal service fund would extend a form of common carrier regulation to competitive, previously non-regulated businesses.**

  -- The Order, for the first time, imposes identical regulatory obligations on common carriers and private service operators -- an outcome clearly at odds with the deregulatory policies that Congress embodied in the Telecomunic-ations Act.

  -- Imposing USF payment obligations on private service operators could encourage and facilitate imposition of other forms of common carrier regulation by State and foreign regulatory authorities.

- **Requiring systems integrators to make payments directly to the universal service fund would not be competitively neutral; it will result in double counting**

  -- Requiring system integrators to make payments to the USF is not necessary to promote competitive neutrality.

  + Systems integrators do not compete against common carriers by providing stand-alone telecommunications services.

  + Rather, they offer service packages that may include consulting, network design and management, enhanced services, data processing, software applications, and computers and customer premises equipment.

  + Telecommunications typically is an incidental part of a systems integrator's offerings.

-- In any case, the payment mechanism adopted in the Order is not competitively neutral. Rather, it will result in systems integrators making "double payments" to the USF.

+ Contrary to the Commission's assumption, because of the existence of long-term contracts, common carriers will not provide capacity to systems integrators at discounted rates.

+ Systems integrators, however, will be required to make payments to the USF on all transactions involving telecommunications.

+ At the same time, systems integrators will not be able to pass these costs on to their customers.

- **The Commission's imposition of universal service payments on non-carriers, including systems integrators, violates congressional intent.**

-- The Telecommunications Act expressly preserves the distinction between common carriers and private service operators.

-- Congress permitted the Commission to require private service operators to make USF payments if the agency determined that network bypass threatens the fund.

-- The Commission has made no finding regarding bypass. Rather, it concluded that -- in the interest of "competitive neutrality" -- private service operators should be treated the same as common carriers. The FCC cannot substitute its judgment for that of the Legislature.

- **Solution I: Limit the universal service fund payment obligation to common carriers.**

-- This approach would eliminate all legal, policy, and administrative issues.

-- This is the approach originally proposed in the House bill and by the Joint Board.

- **Solution II: Do not require systems integrators to make direct payments to the universal service fund.**

  -- Because systems integrators typically do not compete against common carriers, the principle of competitive neutrality does not require that they contribute to the USF.

  -- Systems integrators can be readily distinguished from carriers and other "other telecommunications providers."

  -- This approach would not require major change to the Order.

- **Solution III: Modify the Order to eliminate the "double counting" problem.**

  -- There are at least three ways in which the Commission could eliminate the double counting problem:

  + replace the end-user revenue approach with a "net telecommunications revenue" methodology;

  + require carriers to provide lower rates to systems integrators and other private service operators that reflect the "avoided cost" from not having to make USF contributions based on telecommunications revenues obtained from these entities;

  + require carriers to provide systems integrators and other private service operators with a "fresh look" at existing telecommunications contracts.

  -- While this approach would provide important relief for the near to intermediate term, it would not resolve the long-term legal, policy, and administrative issues.

- **At a minimum, the Commission should limit the January 1998 universal service fund payment obligation to common carriers, and issue a further notice of proposed rulemaking.**

  -- Imposition of USF payment obligation on systems integrators and other private service operators has raised numerous legal, policy, and administrative issues that the Commission did not anticipate.

  -- The Commission should release a further notice of proposed rulemaking in order to develop a more adequate record regarding the imposition of USF payment requirements on non-carriers, including systems integrators.

  -- This approach will not reduce the amount of money available for universal service, and will have a de minimis effect on the size of carriers' initial USF payments.

  -- Pending further action by the Commission, non-carriers would contribute to universal service through payments to their carriers.

Ex Parte Submission of the Ad Hoc Telecommunications Users Group, EDS Corporation, the Information Technology Association of America, and International Business Machines Corporation, CC Docket 96-45

THE COMMISSION SHOULD RECONSIDER ITS DECISION TO IMPOSE UNIVERSAL SERVICE PAYMENT OBLIGATIONS ON SYSTEMS INTEGRATORS

SYSTEMS INTEGRATORS PROVIDE MANAGED DATA PROCESSING AND INFORMATION SERVICE PACKAGES; ANY TELECOMMUNICATIONS IS AN INCIDENTAL PART OF THEIR INTEGRATED OFFERINGS

Systems integrators are providers of managed data processing and information services packages that may include network design and management, information and enhanced services, computers and customer premises equipment, data processing, and software applications. Systems integrators may provide telecommunications to third parties: (1) as an incidental part of their integrated offering, and not on a stand-alone basis; (2) over facilities provided by common carriers; and (3) pursuant to individually negotiated private contracts.

THE PRINCIPLE OF "COMPETITIVE NEUTRALITY" DOES NOT REQUIRE THAT SYSTEMS INTEGRATORS MAKE DIRECT PAYMENTS TO THE USF

The Commission's concern about competitive neutrality is not applicable to systems integrators because systems integrators do not compete against providers of stand-alone telecommunications services. In antitrust terms, "systems integration" and "telecommunications" services are not in the same relevant market. Customers do not view systems integration services as a substitute for telecommunications. See Department of Justice-Federal Trade Commission Merger Guidelines § 1.11. Indeed, it would not be economically rational for a customer to contract with a systems integrator solely to obtain telecommunications. Consequently, neither telecommunication providers nor systems integrators "base business decisions on the prospect of buyer substitution between [these services] in response to changes in price or other competitive variables." Id.

SYSTEMS INTEGRATORS CAN BE READILY DIFFERENTIATED FROM OTHER ENTITIES THAT WILL MAKE DIRECT PAYMENTS TO THE USF

Systems integrators can be readily differentiated from other entities who will be required to make direct payments to the USF. Unlike telephone companies, systems integrators do not own telecommunications facilities. And, unlike resellers, they are not common carriers. Rather, systems integrators are a type of enhanced service providers. The fact that these operators provide incidental telecommunications as an incidental part of their integrated offering does not alter the enhanced status of the entire offering. See Amendment to Section 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry), Phase II Reconsideration Order, 3 FCC Rcd 1150, 1170 n.23 (1988) (subsequent history omitted). Under the Telecommunications Act, firms may not be required to contribute based on revenues from enhanced services.

THIS PROPOSAL WOULD NOT REDUCE THE SIZE OF THE USF, AND WOULD HAVE VIRTUALLY NO IMPACT ON THE SIZE OF CARRIERS' USF PAYMENTS

The size of the USF will remain the same. Moreover, eliminating the requirement that systems integrators make direct payments to the USF would have almost no impact on the size of the carriers' USF payments. While precise data is not available, we estimate that carrier contributions would increase by no more than one-quarter of one percent. At the same time, systems integrators will make significant contributions to universal service through the rates they pay to the facilities-based carriers from which they obtain service.